

“GMM Pfaudler Limited Q1 FY18 Earnings Conference Call”

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Management: **Mr. Tarak Patel – MD, GMM Pfaudler**
Mr. Ashok Pillai – COO, GMM Pfaudler
Mr. Jugal Sahu – CFO, GMM Pfaudler
Ms. Mittal Mehta – Company Secretary, GMM Pfaudler

Moderator: Ladies and gentlemen good day and welcome to the GMM Pfaudler Limited Q1 FY18 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call please signal the operator by entering ‘*’ then ‘0’ on your touchtone phone. Please note that this conference is being recorded. I now hand the conference to Mr. Diwakar Pingle from Christensen. Thank you and over to you Diwakar.

Diwakar Pingle Thank you Mellissa. Welcome everyone and welcome to this Q1 FY 18 Earnings for GMM Pfaudler Ltd. Please note that the results have been mailed to you and you can also view this on our website and also the stock exchange where it has been uploaded. To take us through the results of this quarter and to answer your question we have the management team represented by Mr. Tarak Patel – Managing Director, Mr. Ashok Pillai – Chief Operating Officer, Mr. Jugal Sahu – Chief Financial Officer and Mrs. Mittal Mehta – Company Secretary. We will start the presentation with brief overview of the quarter gone past given by Mr. Tarak Patel, after which we will dive into the Q&A session.

I would like to remind you that everything that is said on this call that reflects any outlook for the future which can be constituted as forward-looking statement must be viewed in conjunction with the risks and uncertainties that we face. These uncertainties and risks are included but not limited to what we have mentioned in the

prospectus filed with SEBI and subsequent annual report which you can find on the website.

With that said I will now hand over the call to Mr. Tarak Patel. Over to you.

Tarak Patel

Thank you Diwakar. Welcome ladies and gentlemen, let me just quickly take you through our Q1 results.

So, talking about GMM Pfaudler for the standalone figures, the revenues has grown by 19% standing at INR 74.1 crores for this current quarter as compared to INR 62.2 crores in the same quarter last year. Our operating expenses have increased by 3 % year on year and has gone from INR 53.5 crores to INR 66.3 crores. The main reason for the increase in the operating expenses has been that we have produced more equipment this year and our electric consumption has also increased.

We are also in the process of running few major improvements where we are hiring outside consultants to come in and do some work for us. So there has been some cost and the expenses have increased on that front as well. The EBITDA is down 8% year on year; however PBT and PAT on year to year basis have increased by 4 %. Having said that the outlook of the year still remains strong, we have a strong backlog on most of our product line. There is continued investment from Pharmaceutical and the chemical companies they continue to invest in new facilities as well as upgrading the factories so business is looking good and we are on target of maintaining our revenue and profit numbers for the year.

Our subsidiary Mavag has also done well. Obviously, the numbers have not been incorporated but they have grown both revenue and profitability this quarter. So having said that floor is open for questions and Diwakar we can have it open for questions please.

Diwakar Pingle

Sure. Mellissa go ahead and open the floor for Q &A please.

Moderator

Thank you. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Vijay S. Gala from Gala Consultancy. Please go ahead.

Vijay Gala

Sir one thing I want to know about that as far as Heavy Engineering is concerned, how much turnover we will be producing this year? Order positions in Heavy Engineering.

Tarak Patel

So Heavy Engineering is the new business area for us and you know we expect the Heavy Engineering to be a big chunk of our total revenue. We expect to grow that business line for at least double digits but to be and I would not like to share number for the year but we definitely want to grow the business, it's a focus area and should grow faster than the other business line.

Vijay Gala

So what do you expect for 2020? Is there a vision as far as 2020?

Tarak Patel

Well as per our strategic plan you know we expect our non-Glass Lined business to be 50% of the revenues right now it's about 30%. So, we need to grow that so the Glass Lined and non-Glass Lined both of which will equal to 50% of our total revenues.

Vijay Gala

Okay sir. So, this quarter also your raw material cost increased, what will refer to the other product point of view margin?

Tarak Patel

So the material cost in the single quarter, the phenomenon because we buy plates a few quarters in advance, so this quarter we actually used plates which were more expensive than the order that has come in, we see that changing over the next quarter and we will get benefit of the lower materials cost going forward.

Moderator

Thank you. We have the next question from the line of Sunil Jain from Nirmal Bang Securities. Please go ahead.

Sunil Jain

My question more relates to other expenses which has increased substantially. The last year it was around INR 6.5 crores that has gone to INR 15 crores so can you identify any specific thing in that. You mentioned consultant fees and all, is it possible to quantify that?

Tarak Patel

Sure so I will give you a small breakup, so in terms of consultancy fees we have actually we are running a very important manufacturing improvement program where we trying to increase our production from about 1400 units to about 2000 units. For that we are using a consultant, Alvarez and Marsal and this is a six month ongoing thing which will cost about, so this quarter is taken about INR 6 million or INR 60 lacs of expenses on that, plus we have some foreign Consultants who are helping us improving our engineering, so that also has accounted about INR 3 million worth of expenses plus we have electric expenses that have increased because we have actually produced 50 more units compared to last quarter. And these extra units have increased our electric consumption so that accounts for about INR 8 million. Our natural gas prices have also increased also by INR 2 million. So, in total we spend about INR 3 crores of additional expenses which were not normal course of business.

Sunil Jain

Yes but this power cost which we spent must be regular or operational?

Tarak Patel

So normally when we produce most of our units are produced in the gas the powered furnaces however there is increase in the production, we are increasing the total number of units that we have produced and hence we have to use the electric furnaces which we normally don't use and because of that the cost has increased.

Sunil Jain

So with the help of this consultant what type of benefit we are likely to get apart from increasing the number of units which you can produce, is there any scope for reduction in cost?

- Tarak Patel** Yes there is a cost reduction program as well the number of units and I mean improving the efficiencies throughout the factories, so there will definitely be cost benefits as well.
- Sunil Jain** And whether is it possible for you to quantify your order booking or period you are booked for?
- Tarak Patel** So I mean we don't quantify our order backlog that is some information we don't share but we are in a very strong position and not only in our single product line but in all our business line and we are confident of meeting the number that we have planned for this year so, we are in a very strong position and the order backlog is very robust.
- Sunil Jain** And sir about the export of these Glass Lined products, we initially dispatched few vessels to Pfaudler. So have we got any further order in that or how is the progress over there?
- Tarak Patel** You are talking about the units that we have sold to Pfaudler?
- Sunil Jain** Yes.
- Tarak Patel** Yes, we have got a repeat business from them as well and that has been quite a success and going forward hopefully that will also increase.
- Sunil Jain** You have already received further order for that?
- Tarak Patel** Yes we have.
- Moderator** Thank you. We have the next question from the line of Aditya Deorah who is an individual investor. Please go ahead.
- Aditya Deorah** Good afternoon sir. Sir have we decided anything on the cash we are having on our balance sheet, I guess it is right now INR 75 crores or so?
- Tarak Patel:** Sorry can you repeat the question please?
- Aditya Deorah** Have we decided anything on the cash that is sitting on the balance sheet that is INR 75 crores or so it is sitting in the balance sheet because if I am not wrong on the consolidated balance sheet?
- Tarak Patel** Obviously we don't want too much cash to be lying on our balance sheet we are in the prospect of looking at acquisition, we have looked around, unfortunately we haven't been able to find something that fits into our product portfolio, but we are always open and hopefully we would be able to deploy the cash in the near term. But having said that we have nothing in our mind right now but we are always open to acquisitions and deploying the cash.

Aditya Deorah

Because sir what happens is, it is decreasing our ROE quite a bit. Like our ROC of our core business is quite high but because of the cash that is sitting on the business the ROE of the entire company is like dragging from the ROE?

Tarak Patel

Right we have talked with the people yesterday also and they were telling us the same thing so yes, we will look in different ways for deploying the cash and improving the ROEs and ROCs.

Aditya Deorah

And sir can you quantify the Mavag numbers even if it's like a what percentage growth has happened in the last first quarter even you don't first quantify it?

Tarak Patel

I couldn't quantify the numbers because they are un-audited but I would say that revenues have increased at least by 60 % or so. And profit is also up by more than 100% so Mavag is doing well and we also have a strong backlog and we also expect to meet the number for the year.

Aditya Deorah

And sir what has fundamentally changed in Mavag over last two years because previously Mavag use to never perform in this particular manner but for last two years something has changed in the company right?

Tarak Patel

See In Mavag, we actually realize that it has a breakeven point of a 10 million Swiss Franc. Anything over that we start making good money, there are looking at India more and more as sourcing low cost components and that model is working well in Europe for them so they have Indian source components which they finish in Europe so the European customer gets the best of both worlds, they get the low cost and they also get the European finish. So that has been quite successful for them and they have also looked at new markets like the US markets where they have had some success and the Chinese market as well. So as long as Mavag meets the revenue numbers anything more than 10 million Swiss Franc then you see a lot of flow through the profitability.

Aditya Deorah

Okay, sir will we benefit because of the government focus right now on bulk drug manufacturing in India as compared to the past?

Tarak Patel

The government focus always has been on the bulk drug but what has change in the recent past is the fact that FDA has come on hard on the big companies who use to be a FDA approved and most of the companies have not expanded but then the purpose of refurbishing and replacing the older equipment's they had with new equipment so we have getting some business from these companies for replacement equipment's.

Aditya Deorah

So maybe because of the FDA actions the enquiry for us has increased for our company has increased in recent past.

Tarak Patel

No they have not, they have changed in terms of, I mean they have not increased they are still strong enquiry from pharma but the enquiries are not for new projects but

typically more replacement of plants and equipment supplied that has supplied to them in the past.

Aditya Deorah

My query was more regarding the China issue most of the bulk drugs if I am not wrong is imported right so the government wanted to manufacture it in India going ahead and the Govt. is trying to incentivize the local producers for the same. So are we ...

Tarak Patel

That is not a great fraction on that, that has been on the safer than that has been discussed for quite some time and they have not talked about given these regions and giving infrastructure support from the government to take away dependence from China but that has not seen traction in major way in the Pharma business. But in the fine chemicals we have seen some traction of that nature with some of plants requiring more core chemical activities coming into the country which was not there in the past not so much in the Pharma sector as yet.

Aditya Deorah

Thank you sir. That's all from my side, all the best for the future.

Moderator

Thank you. We have the next question from the line of Bhavin Chheda from Enam Holdings. Please go ahead.

Bhavin Chheda

Yes good afternoon sir. Sir can you quantify the order book in terms of number of vessels and value?

Tarak Patel

So the order book again is broken up into our three-business line so I can't just base it on number of units or number of vessels but the order book is significant it takes us through pretty much a quite a few months and again as I have said that we are on track and very comfortable to meet the numbers that we have planned for the year.

Bhavin Chheda

And sir what would be your capacity utilization right now in Q1?

Tarak Patel

In Q1 we would be somewhere around 90%.Having said that as I have told you we are working on the manufacturing improvement program so we are looking at revamping some of the internal systems and process, that should have free up some capacity as well. We also have a new gas furnace that is going to come in at the end of the year so that will also add capacity as far as the furnaces goes.

Bhavin Chheda

And in this quarter what would be the export revenues from India to overseas?

Tarak Patel

I think in Q1 we have about export revenue of about INR 60 lakhs so not much, but having said that we do have orders in the pipeline for exports so even though we don't go out and proactively look at exports we are trying to grow our export businesses.

Bhavin Chheda

Okay. Thank you. And best of luck.

Moderator

Thank you. We have the next question from the line of Sunil Jain from Nirmal Bang Securities. Please go ahead.

Sunil Jain

Yes sir one more question, this is more related to the supply which we make to Pfaudler, see over a period let's say in next two to three years how much percentage of revenue we can get from our parent?

Tarak Patel

Good question, the only thing I can say is that they have, even the guys on the ground have, found it quite useful to sell the vessels manufactured from India. They are looking at markets that they are not normally present like the Eastern European markets, the Southeast Asian markets where some of these vessels could go into, so depending on, you know, how quickly they are able to sell this equipment. I see that as business opportunity definitely for the Group and it benefits both GMM Pfaudler as well as Pfaudler globally so I think there will more success in terms of value and quantity. I can't put a number to it right now but going forward I think it is something that it will grow.

Sunil Jain

And sir in this business where we got good growth this time this year no doubt this was quite small of Heavy Engineering, which sector has contributed this growth, from where we got the growth?

Tarak Patel

See growth is from the specialty chemicals and fertilizers as a matter of a fact that's where the two sectors that gave us the biggest growth in Heavy Engineering. And these are historically not our normal sectors so we are diversifying and we are trying to enter in the new markets as well new industry segments. Usually our key industry segments are pharma, Agro and Specialty Chem but these segments also give a good amount of orders this time. The fertilizers and oil and gas are also segments that we are catering to.

Sunil Jain

And sir last question this proprietary product is what? In segment you have given proprietary product?

Tarak Patel

Right so we have created new segment this time, so of course the glass and equipment is one, Heavy Engineering is the business plan we are trying to focus and grow. And Proprietary products includes Mixing Systems, Engineered Systems and Filtration and Drying as the proprietary technology and they are complimentary to Glass Lined equipment's so they are going to the same factories and same industry segment as Glass Lined equipment goes into.

Sunil Jain

Is it somewhere related to Mavag also?

Tarak Patel

Yes. Mavag also does the similar product line Filtration and Drying.

Moderator

Thank you. We have the next question from the line of Nikhil M, an individual investor. Please go ahead.

Nikhil M

Sir the manufacturing improvements program that you have taken up. Will the company also make an investment for the same to take up the capacity from 1400 units to 2000 units?

Tarak Patel

The only capacity that we are trying to increase and we have already placed an order for is the new gas furnace that we are buying that should come at the end of the year but everything else is just going to come through improvements. Improvements in the way that manufacturing process, automation and things like that but not major CAPEX is planned for going 1400 to 2000.

Moderator

Thank you. We have the next question from the line of Rahul Jagwani from SKS Capital. Please go ahead.

Rahul Jagwani

In the beginning you mentioned some foreign people who have come in to help to improve engineering or something, can you throw more some light on that what is that exactly?

Tarak Patel

So we have a consultant whose is working with us to help us improve our mechanical drives that go for our mixing systems as well as for our Glass Lined equipments. So, he has lots of experience doing that sort of work heading a very large mixing company. He is retired from there and he is available to us so he is working with us for that support.

Rahul Jagwani

We were opening these small shops in these industrial zones for maintenance so what is the progress on that?

Tarak Patel

We have already commissioned two of them one is Vizag and one at Ankleshwar and we are opening the third one at Roha so with these three centers, which is the spares, sales and support centers that we have, we expect to get a lot of business both in terms of ex-stock availability of spare parts for those centers because all those areas are chemical zone. And we also hope to get some revenue from quick services and we have plan to have service and located there.

Moderator

Thank you. We have the next question from the line of Vijay S. Gala from Gala Consultancy. Please go ahead.

Vijay Gala

Regarding the Heavy Engineering point of view sir how much your order is expected from Engineers India this year?

Tarak Patel

No we are not expecting any specific order from Engineers India because we don't have any specific approvals from them for the type of equipment that they think we should be bidding for and no orders we expect from Engineers India.

Vijay Gala

Pfudler collaborator has a wide variety so what new product that you are going to introduce in India?

Tarak Patel

So Pfudler of course has a wide variety of products in the Glass Lined equipment and as a matter of fact our product range is probably larger than that of Pfudler because we have a lot of non-Glass Lined equipment also as a part of product band. So Pfudler has other companies that are part of a group now. A company called

Montz that does column internals and stuff like that and we are trying to see how we can integrate some of the products that these companies have with what we are offering now. So we are working towards that. It is still early days we don't have anything to report either to the board or shareholders at large but we are working with them to see how we can help each other.

Moderator Thank you. We have the next question from the line of Rishabh Ghia whose is an individual investor. Please go ahead.

Rishabh Ghia I just wanted to probe on the export side as a company do we export outside of Pfaudler's reach as well in the sense you setting up a front-end marketing and selling in other countries?

Tarak Patel So for the Glass Lined business we depend on the Pfaudler network to get us enquiries in key market that they are present in. There are some markets that we directly sell into. The market close to India like Middle east, Africa and Southeast Asia but the US and the European markets are controlled by the Pfaudler and we go through them when we need to quote there. Having said that the other product lines we can go and export to so we are trying to build our export business in our Heavy Engineering and in our proprietary products and in that sense, we don't have any restrictions on exporting.

Rishabh Ghia And how is that initiative coming along? The reason I asked is that if I gathered it right the export number was just partly INR 60 lakhs right on the INR 75 crore base this quarter. How is exports shaping up, because it is my understanding that the export businesses is a high margin business otherwise?

Tarak Patel Right. So the export is always a high margin business we have a lot of opportunities open opportunities currently for the export market having said that the last few years have been slow for the export markets as well, the Middle East oil and gas industry is slow, Europe was also slow and the US was slow as well. Things are looking brighter. There are open opportunities and hopefully we will have some success in some of these opportunities. And obviously the exports are not going to be a very large chunk but it is definitely going to be bigger than last year that was our feeling.

Rishabh Ghia Okay my second question more around the margins could you throw some color on how the margins are with respect to GLE and the Heavy Engineering business which one would be a higher margin business and given the fact that now we are going to have a 50-50 mix at this time but how the margin would be affected on that account?

Tarak Patel So Glass Lined if by far a most profitable business line, however, Heavy Engineering is also is profitable along if you choose the right business. Heavy Engineering Export business, Heavy Engineering high thicknesses, exotic materials, special jobs you do get high margins in and you know you have to create a niche for yourself. In term of

brand name, in terms of accreditation, in terms of engineering capabilities we can differentiate ourselves from the local fabricators. So we had created such a niche for ourselves and we do Heavy Engineering business only when the margins are similar to those of Glass Lined and otherwise we don't really compete. And as you said the export margins are obviously much better. So Heavy Engineering business from export market is something that we are trying to look at. We have participated in exhibitions in the Gulf area. There are opportunities in Sweden and some parts of Europe they also look quite good at the moment. So if hopefully things go the way they should we should also have some growth and that would include the margins.

Rishabh Ghia

Somewhere in the call we discuss about 90% utilization, I agree that we have some debottlenecking going on but do you worry that we are almost fully-utilized?

Tarak Patel

In terms of being fully-utilized no I think if we can hit 2000 units I think we would be good for at least next few years. However, we will have to invest in plants and machinery after 2020 so we would need shed, we would need more space which is available and we are putting up a shed that is not something that takes too long or it is not too expensive. Its only additional factory area that we need besides that we can also look at outsourcing some of the non-core activities to free up some internal capacity.

Moderator

Thank you. We have the next question from the line of Kapil Arora an individual investor. Please go ahead.

Kapil Arora

Actually I wanted to ask whether is there any possibility of increasing the dividend because good amount of cash is there in the balance sheet and whether there is a possibility of bonus share to increase the liquidity.

Tarak Patel

We had a good closing last Q4 so had increased the dividend. Hopefully, this year also we can try and maintain the same kind of level throughout the year. Bonus share that's something that we have not really thought about but it is not something that we won't think about going forward and that something that can be talked about. We have no plans at the moment but going forward we can look at that as one of the ways of deploying the cash we have on our books.

Kapil Arora

And the second question is why there is a so much focus on the Glass Lined because since the growth in the segment is almost flat on quarter-to-quarter?

Tarak Patel

The segmental growth is almost flat yes because as I mentioned that we did produce more units but because of the material cost and the lower price the revenue is pretty much the same but going forward in the next quarters you will see some improvement in that.

Moderator

Thank you. As we have no further questions I would like to hand the floor back to the management for closing comments. Please go ahead.

Tarak Patel

Thank you for joining the call ladies and gentlemen. Just closing comments as I mentioned earlier that we are working on some important things in our factory so hopefully going forward we can be stronger. We are going after market share and that could come at a cost of margin. Having said that, we are also looking at ways of improving our margins, of reducing our costs and looking at the backlog we currently have I think we are at the stronger position to meet the targets that we have set out for the year and the next few years going forward also to look quite promising. Thank you once again and we will probably talk to you in the next quarter Conference Call. Thanks.

Moderator

Thank you gentlemen. Ladies and gentlemen on behalf of GMM Pfaudler Ltd. that concludes this Conference Call. Thank you for joining us and you may now disconnect your lines.